

STATE OF TENNESSEE

Office of the Attorney General



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TN REGULATORY AUTHORITY  
DOCKET  
**MICHAEL E. MOORE**  
SOLICITOR GENERAL

CORDELL HULL AND JOHN SEVIER  
STATE OFFICE BUILDINGS

TELEPHONE 615-741-3491  
FACSIMILE 615-741-2009

October 17, 2002

Chairman Sara Kyle  
Tennessee Regulatory Authority  
460 James Robertson Parkway  
Nashville, Tennessee 37243

**RE: IN RE: UNITED CITIES GAS COMPANY, a Division of ATMOS ENERGY  
CORPORATION INCENTIVE PLAN ACCOUNT (IPA) AUDIT  
Docket No.: 01-00704**

Dear Chairman Kyle:

Enclosed is an original and thirteen copies of the Office of the Attorney General's Second Supplemental Response to First Data Requests from United Cities Gas Company in the above-referenced matter. We request that this be filed in this docket. Please be advised that all parties of record have been served copies of these documents. If you have any questions, kindly contact me at (615) 532-3382. Thank you very much.

Sincerely,

A handwritten signature in cursive script that reads "Shilina B. Chatterjee".

Shilina B. Chatterjee  
Assistant Attorney General

Enclosures

59338

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**IN RE:** ) **DOCKET NO. 01-00704**  
 )  
**UNITED CITIES GAS COMPANY, a** )  
**Division of ATMOS ENERGY** )  
**CORPORATION INCENTIVE PLAN** )  
**ACCOUNT (IPA) AUDIT** )

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**SECOND SUPPLEMENTAL RESPONSE TO FIRST DATA REQUESTS  
FROM UNITED CITIES GAS COMPANY**

---

The Tennessee Office of the Attorney General, through the Consumer Advocate & Protection Division ("Attorney General"), hereby supplements its response to United Cities Gas Company's ("UCG") First Data Requests.

The TRA Rules provide that discovery should be conducted in accordance with the Tennessee Rules of Civil Procedure. Therefore, these supplemental responses are provided pursuant to Tennessee Rules of Civil Procedure. The Attorney General supplements its response as follows:

2. Identify the factual basis of and any and all documents which refer and/or relate to the statement on Page 13 of the memorandum that "UCG considered transportation delivery costs and they considered them to be incidental to commodity costs."

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TN REGULATORY AUTHORITY  
DOCKET ROOM

**IN RE:** ) **DOCKET NO. 01-00704**  
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**UNITED CITIES GAS COMPANY, a** )  
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2. Identify the factual basis of and any and all documents which refer and/or relate to the statement on Page 13 of the memorandum that "UCG considered transportation delivery costs and they considered them to be incidental to commodity costs."

**SUPPLEMENTAL RESPONSE:** After making a reasonable inquiry to provide a meaningful response to this request while not representing that this answer is an exhaustive listing of every conceivable fact that may be responsive to this request, the Attorney General supplements their previous response with the following: In docket 97-01364, UCG entered a report prepared by Andersen Consulting dated February 28, 1997 concerning the experimental performance-based ratemaking mechanism for the period of April 1, 1995 to November 30, 1996. Attached as Exhibit A. This report provides further evidence that transportation delivery costs were considered incidental to commodity costs.

4. With respect to Page 14 of the Memorandum, identify the factual basis of and any and all documents which refer and/or relate to the statement that "At the time the PBR was filed with the TRA, UCG had no intention of including negotiated transportation discount contracts and did not incorporate them into the PBR."

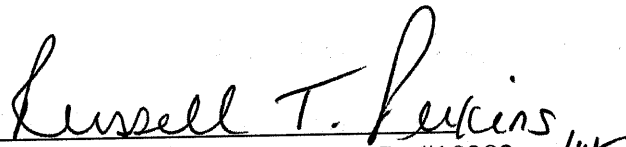
**SUPPLEMENTAL RESPONSE:** After making a reasonable inquiry to provide a meaningful response to this request while not representing that this answer is an exhaustive listing of every conceivable fact that may be responsive to this request, the Attorney General supplements their response with the following additional material: The direct testimony of UCG's witness, Ron W. McDowell on behalf of UCG in TRA docket # 97-1364 dated August 13, 1997 provides additional support for the fact that UCG had no intention of including negotiated transportation discount contracts and did not incorporate them into the PBR. Mr. McDowell stated (Pg. 13, Line 17):

"We knew that TGP [Tennessee Gas Pipeline] was a high cost pipeline, that its rates were something

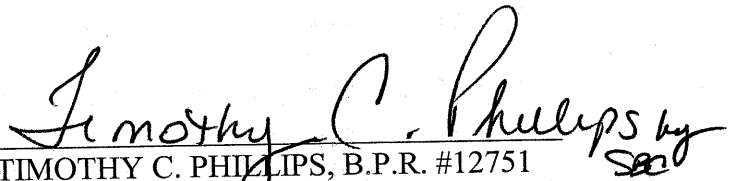
we could not control (say, negotiated down), and we anticipate this situation to continue if not worsen.

Exhibit B attached hereto.

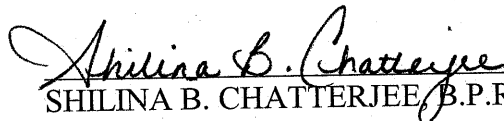
RESPECTFULLY SUBMITTED,



RUSSELL T. PERKINS, B.P.R. #10282  
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Office of the Attorney General  
Consumer Advocate and Protection Division  
(615) 741-1376



TIMOTHY C. PHILLIPS, B.P.R. #12751  
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SHILINA B. CHATTERJEE, B.P.R. #20689  
Assistant Attorney General  
Office of the Attorney General  
Consumer Advocate and Protection Division  
P.O. Box 20207  
Nashville, Tennessee 37202-0207  
(615) 532-3382

Dated: October 17, 2002

## CERTIFICATE OF SERVICE

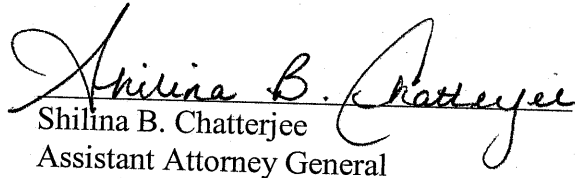
I hereby certify that a true and correct copy of the foregoing was served via facsimile (with copy by U.S. Mail) and/or hand delivery on October 17, 2002.

Sara Kyle  
Chairman  
Tennessee Regulatory Authority  
460 James Robertson Parkway  
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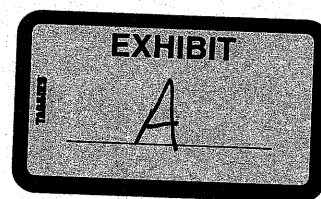
  
Shilina B. Chatterjee  
Assistant Attorney General

# United Cities Gas Company

Second-Year Review of  
Experimental Performance-Based  
Ratemaking Mechanism: April 1, 1995 - November 30, 1996

February 28, 1997

ANDERSEN  
CONSULTING



**United Cities Gas Company**  
**Second Year Review of Experimental Performance-based Ratemaking Mechanism**  
**April 1, 1995 - November 30, 1996**

**Summary of Ratemaking Mechanisms**

Incentive Mechanism		Sharing Arrangement			Performance Indicator		
		Proposed	Approved		Proposed	Approved	
			1 <sup>st</sup> Year	2 <sup>nd</sup> Year		1 <sup>st</sup> Year	2 <sup>nd</sup> Year
1.	Gas Procurement	50/50	50/50	NC	Gains-100% of Indexes  Penalties - 104% of Indexes	Gains - 98% of Indices.  Penalties - 102% of Indices	NC  NC
2.	Seasonal Pricing Differential	50/50	90/10	50/50	Arbitrage between interseasonal prices per futures contracts	As proposed	NC
3.	Storage Gas Commodity	50/50	90/10	50/50	Arbitrage between intraseasonal prices per futures contracts	As proposed	NC
4.	Transportation Capacity Cost	70/30	90/10	(a)	Excess capacity	As proposed	NC
5.	Storage Capacity Cost	70/30	90/10	(a)	Excess capacity	As proposed	NC
Gain/Loss Limitation		\$0	\$25,000/month	\$600,000/year			

a) 90/10 for the first \$500,000 earned from both #4 and 5 mechanisms, and 80/20 thereafter, subject to the earnings cap.

NC = No change

**Mechanism 1: Gas Procurement Incentive** - UCG retains 50% of the savings of the gas purchased below a predefined benchmark. UCG also pays 50% of the costs of the gas purchased above a predefined benchmark. For the purposes of this report, the predefined benchmark is 98% for gains and 102% for penalties. Gains and penalties are determined by four indexes (described below). When gas purchases fall between 98% to 102% of these indexes, no gains or penalties are calculated.

Each gas purchase is assigned to one of six procurement categories:

- Spot purchases made at the beginning of the month
- Swing purchases made during the month
- Long-term spot upstream purchases made under firm term purchases greater than one month
- Long-term swing upstream purchases made under firm term purchases greater than one month
- Long-term spot city-gate purchases made under firm term purchases greater than one month



United Cities Gas Company  
Second Year Review of Experimental Performance-based Ratemaking Mechanism  
April 1, 1995 - November 30, 1996

### III -- FINDINGS

This chapter is arranged in three sections. The first section summarizes UCG's performance during the first year of the program (Prior Period) followed by a review of the results of UCG's gas purchases during the current review period (Current Period). The second section reviews organizational policies and practices and the third section provides an overview of selected utilities with gas procurement incentive programs.

#### A - GAS PURCHASES/CAPACITY RELEASE ACTIVITIES

##### Prior Period

Based on a review of UCG's work papers that were available following the publication of our first report on February 2, 1996, the performance of the plan during its first year of operation, April 1, 1995 through March 31, 1996, was as follows:

April 1, 1995 through March 31, 1996 12-Month Reporting Period				
Incentive Mechanism	Sharing Percent (%)	Total Net Revenue (\$000)	Total Co. Revenue (\$000)	Monthly Avg. Co. Revenue (\$000)
1. Gas Procurement	50/50	\$1,135	\$567	\$47
2. Seasonal Pricing Differential	90/10	\$0	\$0	\$0
3. Storage Gas Commodity	90/10	\$0	\$0	\$0
4. Transportation Capacity Cost	90/10	\$620	\$61	\$5
5. Storage Capacity Cost	90/10	\$0	\$0	\$0
<b>Total</b>		<b>\$1,755</b>	<b>\$628(a)</b>	<b>\$52</b>
Gain/Loss Limitation		\$25,000/month		

(a) Due to the earnings cap, only \$297,000 of the \$628,000 was distributed to UCG. The balance was allocated to the ratepayers.

**Findings:** *Net revenues for the first year of the plan totaled \$1,755,000, the amount available to be split between the ratepayers and UCG, subject to the earnings cap.*

*UCG "out-earned" the monthly cap in 9 of the 12 months of the reporting period.*

*UCG "earned" \$628,000 for the period but those earnings were "capped" at roughly \$297,000.*

*Ratepayers "earned" \$1,458,000 during the reporting period or 83% of the total amount available from the sharing mechanism and the amount in excess of UCG's earnings limitation.*

REDACTED VERSION

BEFORE THE  
TENNESSEE REGULATORY AUTHORITY

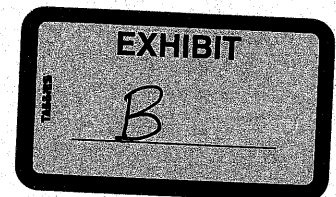
In Re: Application of United Cities Gas )  
Company to Establish an Experimental )  
Performance-Based Ratemaking )  
Mechanism )

Docket No. 97-1364

PREPARED DIRECT TESTIMONY  
OF  
RON W. McDOWELL

ON BEHALF OF  
UNITED CITIES GAS COMPANY

August 13, 1997



REDACTED VERSION

1 contain East Tennessee Pipeline transportation costs, it is the "avoided cost" of  
2 transportation on TGP which is the primary savings. Comparing NORA firm gas cost  
3 into the East Tennessee Pipeline versus Gulf coast gas cost plus TGP transportation cost  
4 delivered into East Tennessee Pipeline provides a true comparison of value to the  
5 customer. *The Gas Procurement Mechanism was specifically designed to recognize the*  
6 *savings with NORA-type transactions.* This transaction is the fourth type of Gas  
7 Procurement incentive calculation within Exhibit RWM-1.

8 Q.

9 \_\_\_\_\_?

10 A.

11 \_\_\_\_\_  
12 \_\_\_\_\_  
13 \_\_\_\_\_  
14 Q. Were changes (increases) to TGP's transportation rates outside the original  
15 expectations of the mechanism?

16 A. No, that is why we have an avoided costs adjustment. United Cities contracted for  
17 NORA gas in order to avoid TGP's high transportation costs. *That is, we knew that*  
18 *TGP was a high cost pipeline, that its rates were something we could not control (say,*  
19 *negotiate down), and we anticipated this situation to continue if not worsen since this*  
20 *was the time period when TGP was negotiating with FERC to impose additional GSR*  
21 *(Gas Supply Realignment or transition) costs resulting from FERC Order 636. We*

REDACTED VERSION

1 knew that TGP's rates could go up, and they did. Absent NORA, our customers would  
2 have incurred higher rates as a direct result of the FERC's GSR decision.

3 **Q. If TGP's rates were outside the Company's control, why then should United Cities**  
4 **benefit from a change in those rates?**

5 A. If we could control TGP's rates that would violate the criteria of an external,  
6 independent benchmark. *What we could do was try to control the amount of*  
7 *transportation we needed on TGP. We did that by shifting to the NORA source of*  
8 *supply.* The fact that the costs we avoided, TGP's transportation costs, did increase  
9 only justifies the reward to the Company because *we recognized the upside risk*  
10 *(increased rates) and successfully avoided that risk,* thereby saving our customers'  
11 money.

12 **Q. In this sense is NORA different from any other long term contract?**

13 A. No. Any time we sign a long term contract, we are, in part, trying to recognize and  
14 shield our customers from the upside risk of rising prices. NORA is no different.

15 **Q. Do you have any further comments about NORA?**

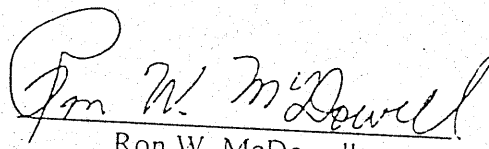
16 A. Yes. From the outset of the PBR, the TPSC acknowledged the Company's ongoing gas  
17 purchasing program and adjusted the reasonableness zone to account for the existence  
18 of NORA in our gas supply portfolio. It is unfair to now change one component of the  
19 standard of measurement (implement a NORA "net margin cap") just because the  
20 performance of our NORA long term contract improved relative to the benchmark.

21 **Q. Please address Mr. Creamer's Recommendation #4 - Delete NYMEX index when it**  
22 **is "off-market."**

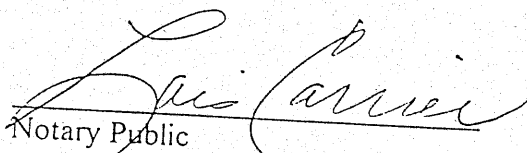
STATE OF TENNESSEE  
WILLIAMSON COUNTY

)  
)  
) ss.

Ron W. McDowell, being first duly sworn deposes and says that he is the Ron W. McDowell referred to in the document entitled "Prepared Direct Testimony of Ron W. McDowell" in Docket No. 97-1364 before the Tennessee Regulatory Authority, and that the statements therein were prepared by him or under his direction and are true and correct to the best of his information, knowledge and belief.

  
Ron W. McDowell

Sworn to and subscribed  
before me this 13<sup>th</sup>  
day of August, 1997.

  
Notary Public

My Commission Expires:

July 24, 1999